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International Tax Bytes by Steve Towers

"International tax news, explained"

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27 January 2023

HIGHLIGHTS

- **Simmering trade tension between EU and US**
  - **Due to "green" tax incentives in Inflation Reduction Act**
- **Countdown of top 10 international tax cases of 2022**

HAPPY FRIDAY!

Germany changes its spots and sends leopards; **Portugal** shows a white card; and an **asteroid** gets really close!

Meanwhile, in the tax world...

Fabrizia deputises; **Nigeria** and **Kenya** want to reduce scope; the **EU** is green with envy; the **Netherlands** allows a mismatch; the **UAE** surprises no-one; **Ethiopia** expands and upgrades; and **Brazil** withdraws credits!

But at the end of the week, the most important question is this: **"Have you shown anyone a white card today?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

(For ITB video subscribers, please log in to access the video and documents/reports)

1. Pillars One & Two
2. Trade & other global developments
3. Top 10 international tax cases in 2022
4. Europe
   - EU, Italy, Netherlands
5. Africa
   - Ethiopia
6. Middle East & Central Asia
   - UAE
7. Americas
   - Brazil, Peru, US
8. Treaty news

ITB series on Pillar One

- **Draft MLC provisions for commitments on DSTs and other relevant similar measures (ITB, 6 January 2023)**
- **Consultation document on Amount B in Pillar One (ITB, 16 December 2022)**
- **Progress Report on Amount A in Pillar One (ITB, 22 July 2022)**
- **Draft model rules for Amount A in Pillar One:**
  - **Tax certainty (ITB, 10 June 2022)**
  - **Regulated Financial Services exclusion from scope (ITB, 13 May 2022)**
  - **Extractives exclusion from scope (ITB, 22 April 2022)**
  - **Scope (ITB, 8 April 2022)**
  - **Tax base determinations (ITB, 25 February 2022)**
  - **Nexus and revenue sourcing (ITB, 11 February 2022)**
- **Inclusive Framework's final agreement on Pillars One & Two (ITB, 15 October 2021)**

ITB series on Pillar Two

- **GloBE Implementation Framework:**
  - **Tax Certainty for the GloBE rules (ITB, 13 January 2023)**
  - **GloBE Information Return (ITB, 13 January 2023)**
  - **Guidance on Safe Harbours and Penalty Relief (ITB, 6 January 2023)**
- **GloBE model rules:**
  - **Art. 7.4 on ETR computation for Investment Entities (ITB, 2 December 2022)**
  - **Corporate Restructurings and Holding Structures (Parts 1 to 7) (ITB, 23 & 30 September; 7, 14 & 21 October; 11 & 18 November 2022)**
  - **Scope (parts 1 & 2) (ITB, 24 June; 1 July 2022)**
  - **Charging Provisions (Parts 1 to 5) (ITB, 6, 13 & 20 May; 10 & 17 June 2022)**
  - **Computation of Effective Tax Rate and Top-up Tax (Parts 1 to 6) (ITB, 18 & 25 March; 1, 8, 22 & 29 April 2022)**
  - **Flow-through Entities and Hybrid Entities (ITB, 4 March 2022)**
  - **Computation of Adjusted Covered Taxes (Parts 1 to 9) (ITB, 11, 18 & 25 February; 29 July; 5,12,19 & 26 August; 16 September 2022)**
  - **Computation of GloBE Income or Loss (Parts 1 to 4) (ITB, 7, 14, 21 & 28 January 2022)**

WORTH READING

Allison Christians and Stephen E. Shay
"The Consistency of Pillar 2 UTPR With U.S. Bilateral Tax Treaties"
Tax Notes Today International, Tax Analysts, 23 January 2023 (posted on LinkedIn by Tax Notes)

Alex M. Parker
"UTPR in the Air: Making Sense of the OECD's Most Controversial New Rule"
19 January 2023 http://www.things-of-caesar.com/ (requires registration, but no paywall)

R.J. de Vries and B.M.R. Pijnenburg
"The Dutch Anti-Base Erosion Rule: Recent Developments in the Context of Fraus Legis and EU Law"
Finance and Capital Markets, IBFD, 2022 (Vol. 23), No. 4 (subscription service)

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo, a company located in jurisdiction A, is a Constituent Entity in an MNE Group which is "within scope" of the GloBE rules. ACo is the only Constituent Entity located in jurisdiction A.

ACo carries on a manufacturing business in jurisdiction A, and is provided with a tax incentive under the jurisdiction A tax law.

ACo is trying to determine how the tax incentive should be designed in the future, having regard to the GloBE rules.

For that purpose, it assumes: (1) its GloBE Income will be 1,000; and (2) its Substance-based Income Exclusion (SBIE) amount will be 800.

Question 1: If jurisdiction A provides a tax exemption for the SBIE amount (800), and levies a 15% income tax on the remainder of ACo's GloBE Income (200), will there be no Top-up Tax?

Question 2: If the answer to Q1 is that there would be a Top-up Tax, what rate of tax should jurisdiction A levy on the remainder of ACo's GloBE Income (200) to ensure that the Top-up Tax is zero?

For the purposes of these questions, please assume that (apart from the exemption of the SBIE amount) there are no permanent or timing differences between the computation of GloBE Income and the computation of taxable profits under the jurisdiction A tax law.

Answer in next ITB email alert!

LAST WEEK'S QUESTION

XCo, a company located in jurisdiction X, is a Constituent Entity in an MNE Group which is "within scope" of the GloBE rules. XCo, a small manufacturing company, is the only Constituent Entity located in jurisdiction X.

YCo, a company located in jurisdiction Y, is also a Constituent Entity in the MNE Group. YCo is the only Constituent Entity located in jurisdiction Y. XCo and YCo are "sister subsidiaries".

The UPE is located in jurisdiction U.

For 2024, the GloBE rules are in effect in jurisdictions X and Y (for both jurisdictions, both the IIR and UTPR are in effect, but not a QDMTT); however, the GloBE rules are not in effect in jurisdiction U or in any of the other 8 jurisdictions in which the MNE Group has Constituent Entities.

For 2024, XCo has the following financial information (determined in accordance with the Acceptable Accounting Standard used by the UPE in preparing its consolidated Financial Statements) (all in EUR millions):

1. Profit before Income Tax: 1.4
2. Revenue: 9
3. Income tax expense (100% Covered Taxes, no "uncertain tax positions"): 0.2
4. Negative adjustments (i.e., reductions) (under Art. 3.2 and following) in computing GloBE Income (note: there are no positive adjustments): (0.5)
5. Adjusted Covered Taxes: 0.1
6. Substance-based Income Exclusion: 0.6

And for 2024, YCo has the following financial information (determined in accordance with the Acceptable Accounting Standard used by the UPE in preparing its consolidated Financial Statements) (all in EUR millions):

1. Profit before Income Tax: 1.2
2. Revenue: 15
3. Income tax expense (100% Covered Taxes, no "uncertain tax positions"): 0.1
4. Net positive adjustments (i.e., add-back) (under Art. 3.2 and following) in computing GloBE Income: 2.0
5. Adjusted Covered Taxes: 0.3
6. Substance-based Income Exclusion: 0.4

Based on this information, will either or both of XCo and YCo have a tax liability under the GloBE rules for 2024?

LAST WEEK'S ANSWER

1. Juris. X Top-up Tax

XCo fails the transitional CbCR safe harbour: (i) de minimis test is failed, because Profit before Income Tax is not less than EUR 1m; (ii) simplified ETR test is failed, because simplified ETR is: 0.2 / 1.4 = 14.3%; and (iii) routine profits test is failed, because Profit before Income Tax exceeds SBIE amount.

However, XCo satisfies the de minimis exclusion in Art. 5.5: Average GloBE Revenue = EUR 9m, and Average GloBE Income = EUR 0.9 (see the Commentary's discussion on how to determine the "average" numbers in the first year when GloBE rules apply).

If the election is made (I will assume that it is), Art. 5.5 requires that the Top-up Tax for 2024 is zero.

2. Juris. Y Top-up Tax

YCo fails the transitional CbCR safe harbour: (i) de minimis test is failed, because Total Revenue is not less than EUR 10m, and Profit before Income Tax is not less than EUR 1m; (ii) simplified ETR is failed, because simplified ETR is: 0.1 / 1.2 = 8.3%; and (iii) routine profits test is failed because Profit before Income Tax exceeds SBIE amount.

YCo also fails the de minimis exclusion in Art. 5.5: Average GloBE Revenue is not less than EUR 10m, and Average GloBE Income is not less than EUR 1m.

Calculation of Top-up Tax...

GloBE Income: 1.2 + 2.0 = 3.2
ETR: 0.3 / 3.2 = 9.375%
Top-up Tax Percentage: 5.625%
Excess Profits: 3.2 – 0.4 = 2.8
Top-up Tax: 5.625% x 2.8 = EUR 0.1575m

3. UTPR

Art. 9.3 will not apply to exclude the application of the UTPR in 2024, as the MNE Group is not "in its initial phase of its international activity": there are Constituent Entities in more than 6 jurisdictions.

The UTPR of EUR 0.1575m will be allocated between jurisdictions X and Y, according to the allocation formula in Art. 2.6. Note that UTPR for 2024 will be allocated (in part) to jurisdiction X, even though that jurisdiction qualifies for the de minimis exclusion in 2024.

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